

S
351.7232
L.72d h
1976

STATE OF MONTANA

DEPARTMENT OF HIGHWAYS

Report on Examination of Financial Statements

Conducted Under Contract By
Ernst and Ernst, CPA's

Fiscal Years Ended June 30, 1975 and June 30, 1976



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MONTANA
STATE CAPITOL • HELENA

Montana State Library



3 0864 1003 9755 6



STATE OF MONTANA

DEPARTMENT OF HIGHWAYS

Report on Examination of Financial Statements

Conducted Under Contract By
Ernst and Ernst, CPA's

Fiscal Years Ended June 30, 1975 and June 30, 1976

OVERVIEW

AUDIT OF THE DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

June 30, 1976

INTRODUCTION

The audit of the Department of Highways of the State of Montana was a financial compliance audit. The purposes of the audit were to (a) determine whether or not the Department complied with applicable state laws and regulations, and (b) express an opinion as to whether or not the Department's financial statements were fairly presented for the fiscal years ended June 30, 1976 and June 30, 1975. In conjunction with the examination of the financial statements, comments and recommendations were prepared as constructive suggestions to assist the Department in its continuing efforts to improve accounting and reporting procedures.

SUMMARY OF FINDINGS

Compliance with State Laws and Regulations

Based on discussions with appropriate Department personnel and on tests as deemed necessary, the Department appears to be in compliance with pertinent statutes and regulations. Further, the Department appears to be in compliance with recommendations and guidelines contained in the Montana Administrative Manual.

Opinion on the Department's Financial Statements

The Department's financial statements have been presented in a format suggested by groups largely responsible for determining recommended governmental accounting

and reporting practices. This format is new for the Department and is significantly different from the format traditionally followed by the Department. The new format reports the financial activities of the Department so as to better demonstrate the purpose of the individual funds or groups of funds. Note A on page 37 of the report fully describes the purpose of each fund. Opinions expressed on the financial statements of the various funds are as follows:

	<u>Unqualified Opinion</u>	<u>Qualified Opinion</u>	<u>Adverse Opinion</u>
Earmarked Revenue Fund			X
Special Revenue Funds:			
Federal and Private Revenue			X
Coal Area Highway Improvement			X
Intragovernmental Service Funds:			
Motor Pool			X
Equipment Bureau			X
Trust and Agency Funds:			
Highway Agency Account (GVW)	X		
City and County Construction	X		
Retirees' Health Insurance	X		
Outdoor Sign Control	X		

An unqualified opinion means that the financial statements present fairly, in conformity with generally accepted accounting principles, the financial position and results of operations of a fund.

A qualified opinion means that the financial statements present fairly, in conformity with generally accepted accounting principles, the financial position and results of operations of a fund, except for the specific reason(s) indicated.

An adverse opinion means that the financial statements do not present fairly, in conformity with generally accepted accounting principles, the financial position of a fund, or the results of its operations because of the significance of the reasons or exceptions indicated.

Exceptions which caused qualified or adverse opinions were principally related to the Department not following generally accepted accounting principles, or to oversights by the Department in not adjusting certain accounts on a timely basis and in accordance with principles normally followed by the Department.

Comments and Recommendations

There are 26 recommendations in the report. The Department fully concurs with 24 of the recommendations, partially concurs with one recommendation and does not concur with one recommendation. The full text of all comments and recommendations appears on pages 2 through 15. The full text of the Department's written responses appears on pages 45 through 50.

The recommendations made to the Department can be summarized into the following major areas of concern:

o Generally Accepted Accounting Principles

Users of financial statements of governmental units are demanding more and more that statements be prepared in accordance with generally accepted accounting principles.

These principles are being formulated by various authoritative bodies. The Department needs to carefully consider

the applicability of new pronouncements from these bodies.

Financial reporting needs to be adjusted accordingly.

Adjustments may very well be in conflict with existing
SBAS recommendations.

o Personnel Training

In today's accounting and reporting environment it is necessary for all key personnel in any accounting organization be totally familiar with their own responsibilities. It is also necessary for them to have a full knowledge of how their responsibilities fit in with the organization's final product--financial statements. The Department needs to establish routine training programs to thoroughly familiarize each key person in the accounting organization with his or her own responsibilities, the responsibilities of those whom they supervise and with generally accepted accounting and reporting principles relating to their own area of work.

o Internal Accounting Controls

Strong internal accounting controls are important in determining the level of reliance which can be placed on financial statements. Although no significant weaknesses were observed, recommendations were made which would strengthen controls in the areas of:

- . Preparation and review of journal entries
- . Collections from special fuel permit fines
- . Control over unused CWV permit tickets
- . Allowable emergency sick leave
- . Payroll check distribution

o Current Review of Specific Accounts

It is important that all accounts be reviewed on a routine basis. The reviews are necessary to determine the makeup of the account, the collectibility of the account, whether or not there are errors in the account, or if the account is even necessary. Recommendations were made that accounts be carefully reviewed and analyzed on a current and routine basis. Accounts specifically mentioned related to:

- . Allowance for Possible Doubtful Accounts Receivable
- . Costs to Be Allocated to Projects or Other Departments
- . Unreimbursed Costs for Construction Work in Disaster Areas
- . Property, Plant and Equipment
- . Retirees' Health Insurance Fund
- . City and County Construction Fund
- . Gross Vehicle Weight Division Collections
- . Accrued Payroll

OTHER MATTERS OF INTEREST

Compliance with Statewide Budgeting and Accounting System

The Department maintains its own computer and accounting system, which is separate from the statewide accounting system, in order to provide additional accounting and financial management information. The Department follows the statewide budgeting system. Such budgeting system does not result in appropriate relationships to the financial statements prepared from accounts maintained in the Department's accounting system.

State Highway Building Construction Project

For internal purposes, the Department is accounting for costs and debt related to the construction of a new Department of Highways building complex. The state has issued general obligation bonds to finance the project. The

Department does not have responsibility to account for either the project or the related financial arrangements. Such accounting is the responsibility of other state accounting funds.

Property, Plant and Equipment

Generally accepted accounting principles require that a separate General Fixed Assets group of accounts be established to account for property, plant and equipment (fixed assets) except for those accounted for in the Motor Pool Fund and the Equipment Bureau Fund. The Department should as soon as possible, and with proper approval of appropriate state officials, establish separate accounts to account for the fixed assets currently being accounted for in its Earmarked Revenue Fund.

Prior Audit Recommendations

Recommendations contained in the last audit report (year ended June 30, 1974) have been substantially complied with.

CONCLUSION

The Department's early implementation of many recommendations and favorable response to all comments and recommendations indicate a desire to fully conform with generally accepted accounting principles, institute meaningful personnel training programs, strengthen internal accounting controls and carefully complete timely reviews of all accounts.

Office of the Legislative Auditor



STATE CAPITOL
HELENA, MONTANA 59601
406/449-3122

MORRIS L. BRUSSETT
LEGISLATIVE AUDITOR

April 4, 1977

DEPUTY LEGISLATIVE AUDITORS:
JOSEPH J. CALNAN
ADMINISTRATION AND
PROGRAM AUDITS
ELLEN FEAVER
FINANCIAL-COMPLIANCE AND
CONTRACTED AUDITS
STAFF LEGAL COUNSEL
JOHN W. NORTHEY

The Legislative Audit Committee
of the Montana State Legislature:

Transmitted herewith is the report on the audit of the Department of Highways for the years ended June 30, 1975 and June 30, 1976.

The audit was conducted by Ernst and Ernst, Certified Public Accountants, under a contract between the firm and our office. The comments and recommendations contained in this report represent the views of the firm and not necessarily the Legislative Auditor.

The agency's written response to the report recommendations is included in the back of the audit report.

Respectfully submitted,

A handwritten signature in black ink that reads "Morris L. Brusett".

Morris L. Brusett, C.P.A.
Legislative Auditor

Report of Comments and Recommendations
and Audited Financial Statements

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

June 30, 1976

TABLE OF CONTENTS

Appointive and Administrative Officials	iv
Summary of Recommendations.	v
Comments and Recommendations:	
Letter of Transmittal	1
General	2
Generally Accepted Accounting Principles.	2
Personnel Training.	3
Accounting Reports.	4
Interfund Accounting Entries.	4
Review of Journal Entries	5
Fund Equity Accounts.	5
Electronic Data Processing Division (EDP)	6
Allowance for Possible Doubtful Accounts Receivable	7
Costs to Be Allocated to Projects or Other Departments.	7
Unreimbursed Costs for Construction Work in Disaster Areas.	8
State Highway Building Construction Project	8
Property, Plant and Equipment	9
Inventory Receipts and Claims Payable	10
Federal and Private Revenue Fund Accounting	10
Retirees' Health Insurance Fund	11
City and County Construction Fund	11
Gross Vehicle Weight Division Collections	11
Backlog of Computer Input Data.	12
Special Fuel Permit Fines	13
Unused Permit Tickets of the Gross Vehicle Weight Division (GVW)	13
Accrued Payroll	13
Emergency Sick Leave.	14
Payroll Checks.	14
Employee W-2 Forms.	15

Report of Comments and Recommendations
and Audited Financial Statements

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

June 30, 1976

TABLE OF CONTENTS (Continued)

Audited Financial Statements:

Accountants' Report	16
Balance Sheets:	
June 30, 1976:	
Earmarked Revenue Fund.	22
Special Revenue Funds:	
Federal and Private Revenue	22
Coal Area Highway Improvement	22
Intragovernmental Service Funds:	
Motor Pool.	22
Equipment Bureau.	22
Trust and Agency Funds:	
Highway Agency Account.	22
City and County Construction.	22
Retirees' Health Insurance.	22
Outdoor Sign Control.	22
June 30, 1975:	
Earmarked Revenue Fund.	26
Special Revenue Fund:	
Federal and Private Revenue	26
Intragovernmental Service Funds:	
Motor Pool.	26
Equipment Bureau.	26
Trust and Agency Funds:	
Highway Agency Account.	26
City and County Construction.	26
Retirees' Health Insurance.	26
Outdoor Sign Control.	26
Statements of Changes in Equity:	
Year Ended June 30, 1976:	
Earmarked Revenue Fund.	30
Special Revenue Fund:	
Coal Area Highway Improvement	30
Intragovernmental Service Funds:	
Motor Pool.	30
Equipment Bureau.	30

Report of Comments and Recommendations
and Audited Financial Statements

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

June 30, 1976

TABLE OF CONTENTS (Continued)

Audited Financial Statements (Continued):

Statements of Changes in Equity (Continued):	
Year Ended June 30, 1975:	
Earmarked Revenue Fund.	31
Intragovernmental Service Funds:	
Motor Pool.	31
Equipment Bureau.	31
Statements of Revenues and Expenditures:	
Years Ended June 30, 1976 and 1975:	
Earmarked Revenue Fund.	32
Special Revenue Funds:	
Federal and Private Revenue	33
Coal Area Highway Improvement	33
Intragovernmental Service Funds:	
Motor Pool.	34
Equipment Bureau.	34
Statements of Cash Receipts and Disbursements--Trust and Agency Funds:	
Years Ended June 30, 1976 and 1975:	
Highway Agency Account.	35
City and County Construction.	35
Retirees' Health Insurance.	35
Outdoor Sign Control.	35
Notes to Financial Statements	37
Department Replies.	45

APPOINTIVE AND ADMINISTRATIVE OFFICIALS

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

State Highway Commission:

George Vucanovich, Chairman
Wm. M. Kessner, Vice Chairman
Baxter Larson
P.L. Bacheller
John S. Cote

Helena
Great Falls
Wolf Point
Billings
Butte

H.J. Anderson, Director of Highways

Division Administrators:

Jack R. Beckert	Engineering
William A. Blake	Motor Pool and Equipment
LeRoy Broughton	Personnel and Civil Rights
Don Copley	Gross Vehicle Weight
Donald D. Gruel	Maintenance
John L. Prebil	Centralized Services
N.A. Rotering	Legal

SUMMARY OF RECOMMENDATIONS

As a separate section in the front of each audit report we include a listing of all recommendations together with a notation as to whether the agency concurs or does not concur with each recommendation. This listing serves as a means of summarizing the recommendations contained in the report and the audited agency's reply thereto and also as a ready reference to the supporting comments. The full reply of the Department of Highways is included in the back of this report.

Page

Carefully consider the applicability of all authoritative accounting and reporting pronouncements. Accounting systems and procedures of the department should be properly designed to recognize transactions in a manner which would provide for preparation of financial statements in accordance with generally accepted accounting principles. We recognize also that there may be certain limitations imposed by state laws or regulations. Consideration should be given to hiring a person to be specifically responsible during a transition period.

3

Agency Reply: Concur. See page 46.

Institute an overall training program for key accounting employees. At a later date, the program can be expanded to other employees. The program should not be limited to, but should include:

- . Self-study and correspondence courses
- . Formal "classroom" training
- . Courses sponsored by the National Association of Accountants, the American Institute of Certified Public Accountants, the Montana Society of Certified Public Accountants, and other professional organizations
- . Special departmental training programs
- . Periodic rotation of responsibilities

3

Agency Reply: Concur. See page 46.

Continue to monitor the use of and need for reports now being prepared. A current list of available reports should be prepared to include items such as the name of the report, current distribution list, frequency of distribution, and a brief description of the information included in the report. Report users should then be asked to confirm their need for reports received.

4

Agency Reply: Concur. See page 46.

SUMMARY OF RECOMMENDATIONS (Continued)

Page

All persons in the accounting department authorized to make accounting entries should be trained to recognize those entries requiring use of interfund accounts. The entire entry could then be made by the same person, and the time required to analyze the computer summarization could be significantly reduced.

5

Agency Reply: Do not concur. See page 46.

Before being keypunched all journal entries should be properly reviewed by an authorized person. Additional journal entry control could be maintained by having the authorized person approving the entry also control the machine that numbers the entry. No journal entries should be keypunched unless the approval signature and number are present. All journal entry numbers should be accounted for to determine that no prepared entries have been overlooked in the keypunching process.

5

Agency Reply: Concur. See page 50.

The accounting department should not make accounting entries to equity accounts except in unusual and rare circumstances. Any entry that is made to an equity account should specifically relate to an interfund transfer of equity or to the closing of revenue and expenditure accounts at the end of the year. It is suggested that the director of the accounting department be the only person who can approve entries to an equity account.

6

Agency Reply: Concur. See page 47.

Organize a management steering committee to establish policy, evaluate progress, and discuss division problems. The committee should consist of the EDP executive, the manager, and other key Department of Highways executives whose divisions use data processing reports. Minutes of committee meetings should be kept.

6

Agency Reply: Concur. See page 47.

In conjunction with the accounting division, establish special training programs for presentation to users of EDP reports. The programs should be updated on a

SUMMARY OF RECOMMENDATIONS (Continued)

	<u>Page</u>
routine basis. Material in the training programs should not be limited to, but should include: • Description and sample of all reports available • Frequency schedule of times reports are prepared and available • Deadline dates for entering data into the reports • Personnel responsible for various reports • Relationship of reports to each other • Suggested filing system for reports • Suggested length of time to keep the reports on hand	6
<u>Agency Reply:</u> Concur. See page 47.	
An allowance for possible doubtful accounts should be established. To do this, individual accounts receivable should be carefully reviewed at least quarterly. The results of this review, together with historical bad debt trends of the department, should be used as a basis for determining the probable loss from recorded accounts receivable.	7
<u>Agency Reply:</u> Concur. See page 47.	
Unreimbursed costs and reimbursements in excess of costs to be allocated to projects or other departments should be recognized as expenditures or revenues in the proper fiscal period. This does not conflict with the department's overall objective of using these amounts in establishing and/or adjusting billing rates for use of vehicles and equipment.	8
<u>Agency Reply:</u> Concur. See page 47.	
Unreimbursed costs for construction work in disaster areas should be carefully monitored to determine the final disposition of costs incurred. This may necessitate a quarterly listing of costs, by project, and a written status report by the person responsible for the project.	8
<u>Agency Reply:</u> Concur. See page 47.	
Account balances related to the new building complex should, after coordination with other appropriate state officials, be removed from the Earmarked Revenue Fund of the department. The department may desire to maintain a memorandum record of these amounts for management information purposes.	9
<u>Agency Reply:</u> Concur. See page 47.	

SUMMARY OF RECOMMENDATIONS (Continued)

Page

As soon as possible, and with proper approval of appropriate state officials, establish separate accounts to account for the fixed assets currently being accounted for in its Earmarked Revenue Fund. 10

Agency Reply: Concur. See page 48.

Receiving logs with columns for goods received, quantity, vendor name, date, and the person's name who received the goods, should be prepared at each receiving location. The logs, together with appropriate invoices would be sent to the accounting department for processing. These procedures would help ensure that all goods received were placed in highway department inventory (or expenditures), and can be used to determine whether claims payable are recorded in the proper accounting period. 10

Agency Reply: Partially concur. See page 48.

The department's accounting system should be designed to show revenues and expenditures, by type, accumulated between the beginning of a fiscal year and the date reports are prepared. 11

Agency Reply: Concur. See page 48.

The detail ledger showing individual insurance payments made in advance by the retirees should be reconciled to the general ledger on a monthly basis. A file should be kept containing current applications in alphabetical order for each retiree. 11

Agency Reply: Concur. See page 48.

Details of this fund, by city and county, should be reconciled to the general ledger on a continuing basis, preferably monthly. 11

Agency Reply: Concur. See page 48.

Distribution of all collections on a timely basis will give the department's Earmarked Revenue Fund and other governmental units a more timely picture of revenue trends. Reference should be made to the comment entitled Backlog of Computer Input Data. 12

Agency Reply: Concur. See page 49.

SUMMARY OF RECOMMENDATIONS (Continued)

Page

The Earmarked Revenue Fund, based on revenue trends developed from its timely receipt of Highway Agency Account Fund distributions, should institute the policy of accruing this revenue in accordance with generally accepted accounting procedures. 12

Agency Reply: Concur. See page 49.

GVW should consider having its own keypunch operator rather than having to wait for available time from the data processing department. This recommendation also relates to a recommendation under the comment entitled GVW Collections. 13

Agency Reply: Concur. See page 49.

Collections should be sent directly to the highway department accounting office. A copy of the report would also be sent to the GVW division. 13

Agency Reply: Concur. See page 49.

The unused tickets, after being rechecked against the listing of tickets returned, should be more carefully controlled, if not destroyed. This procedure will provide better internal control over the possibility of misuse of tickets. 13

Agency Reply: Concur. See page 50.

Future payroll accruals should be properly recorded as an accrued liability. This procedure is especially important at year end. 14

Agency Reply: Concur. See page 50.

The record system for reporting sick leave should be adjusted to provide information regarding both emergency and regular sick leave. 14

Agency Reply: Concur. See page 50.

The completed payroll checks and payroll journal should be returned from the accounting bureau in Helena to the division manager. The journal could then be returned to the payroll clerk for review. The checks, however, should be distributed by the division manager or another designated employee, but not the payroll clerk or any other employee associated with the hiring

SUMMARY OF RECOMMENDATIONS (Continued)

	<u>Page</u>
process or with the handling of originating payroll records.	14
<u>Agency Reply:</u> Concur. See page 50.	
Returned W-2 forms should be investigated and followed up by employees other than from the payroll department.	15
<u>Agency Reply:</u> Concur. See page 50.	

Ernst & Ernst

850 Lincoln Building • W 818 Riverside Avenue • Spokane, WA 99201 • Phone 509/838-2561

The Legislative Audit Committee
of the Montana State Legislature
Helena, Montana

We have completed our examination of the financial statements of the Department of Highways for the years ended June 30, 1976 and June 30, 1975. Our separate accountants' report on those statements appears on page 16.

Based upon our examination, we submit the accompanying comments and recommendations. They are not in any way intended to reflect upon the honesty or integrity of any employee. They are, however, presented as constructive suggestions to assist the Department of Highways in its efforts to improve accounting and reporting procedures.

We thank the personnel of the Department of Highways for the cooperation we received from them throughout our examination. We would be pleased to discuss the accompanying comments and recommendations with you at your convenience.

Ernst & Ernst

Spokane, Washington
March 11, 1977

ERNST & ERNST

General

The primary legalistic control of the Department's activities rests in the Revised Codes of Montana. In addition, the Department is responsible to follow management memo recommendations and other guidelines contained in the Montana Administrative Manual. Based on our discussions with appropriate Department personnel and on audit tests as we deemed necessary, the Department appears to be in compliance with pertinent statutes and regulations, and with recommendations and guidelines contained in the Montana Administrative Manual.

The last audit report relating to the Department was for the year ended June 30, 1974, and contained twelve recommendations. Our follow-up work indicated that the Department's response and subsequent procedural changes were favorably responsive to ten of those recommendations. One recommendation, concerning excess lands, is being complied with where appropriate as to intensive sales efforts, but has not been complied with (for excessive cost reasons as described in the Department's original response) as to completing current appraisals. Finally, one recommendation, concerning proper approval of journal entries, has not been fully complied with and is included among the recommendations in this report.

Generally Accepted Accounting Principles

Today, three groups are largely responsible for determining recommended governmental accounting and reporting practices: the National Council on Governmental Accounting (NCGA), the AICPA Committee on Governmental Accounting and Auditing (AICPA), and the Financial Accounting Standards Board (FASB). Important authoritative pronouncements from these organizations include Governmental Accounting, Auditing, and Financial Reporting (NCGA), and Audits of State and Local Governmental Units (AICPA). In addition to these two references, Financial Accounting Standards Board pronouncements are also applicable in a broad sense to the Highway Department's accounting and reporting procedures.

Recommendation: The Department should carefully consider the applicability of all authoritative accounting and reporting pronouncements. Accounting systems and procedures of the Department should be properly designed to recognize transactions in a manner which would provide for preparation of financial statements in accordance with generally accepted accounting principles. We recognize also that there may be certain limitations imposed by state laws or regulations. Consideration should be given to hiring a person to be specifically responsible during a transition period.

Personnel Training

We found that the overall accounting responsibilities of the Department were divided among many persons. Each of these persons adequately complete their own assigned tasks, but few of them seemed to understand the relationship of their work to the overall accounting function.

While a wide division of responsibilities adds favorably to the internal control of any accounting organization, we feel this limited employee background of the overall system can lead to unnecessary errors, duplication of efforts, and overall inefficiency. We generally feel that only a few employees, including the administrator of the centralized services division, fully understand the entire accounting system of the Department. Because the administrator is the person most familiar with the system, it is our opinion that he becomes unnecessarily burdened with answering questions, researching problems, etc. This does not allow him the time he rightfully needs to exercise his excellent ability to upgrade reporting systems, change financial statement formats to comply with generally accepted accounting principles, establish training programs, and generally monitor activities of the division.

Recommendation: The Department should institute an overall training program for key accounting employees. At a later date, the

program can be expanded to other employees. The program should not be limited to, but should include:

- o Self-study and correspondence courses
- o Formal "classroom" training
- o Courses sponsored by the National Association of Accountants, the American Institute of Certified Public Accountants, the Montana Society of Certified Public Accountants, and other professional organizations.
- o Special Departmental training programs
- o Periodic rotation of responsibilities

Accounting Reports

In past years memos have been periodically sent to employees requesting comments as to their need of various accounting reports. This procedure has been reported as being effective in reducing the number of reports issued.

Recommendation: The accounting department should continue to monitor the use of and need for reports now being prepared. A current list of available reports should be prepared to include items such as the name of the report, current distribution list, frequency of distribution, and a brief description of the information included in the report. Report users should then be asked to confirm their need for reports received.

Interfund Accounting Entries

Many accounting entries of the Department involve transactions between two or more funds. Several persons authorized to prepare such entries do not seem to be totally familiar with the related interfund accounts.

Consequently, only one side (debit or credit) of some entries is recorded in the general journal. The one-sided entries are then summarized by use of the computer. In turn, the computer summary is separately analyzed to determine the needed corrections and the other side of the entries.

Recommendation: All persons in the accounting department authorized to make accounting entries should be trained to recognize those entries requiring use of interfund accounts. The entire entry could then be made by the same person, and the time required to analyze the computer summarization could be significantly reduced.

Review of Journal Entries

The accounting system provides for proper review and approval of journal entries in advance of their being entered into the accounting records. We noted occasions where advance approval had been made, but review of the final written entry was not made on a timely basis. Lack of timely journal entry review can lead to accounting problems such as postings to wrong accounts, duplicate postings and other serious errors.

Recommendation: Before being keypunched all journal entries should be properly reviewed by an authorized person. Additional journal entry control could be maintained by having the authorized person approving the entry also control the machine that numbers the entry. No journal entries should be keypunched unless the approval signature and number are present. All journal entry numbers should be accounted for to determine that no prepared entries have been overlooked in the keypunching process.

Fund Equity Accounts

Various accounting entries are currently made to the equity accounts of most funds. The described purpose of some of the entries is sometimes unclear and the entries may involve a considerable number of other accounts. According to generally accepted accounting principles, it

would be unusual to post any entry directly to an equity account, other than the year-end closing entry to recognize the excess or deficiency of revenue over expenditures, or the transfer of equity from one fund to another.

Recommendation: The accounting department should not make accounting entries to equity accounts except in unusual and rare circumstances. Any entry that is made to an equity account should specifically relate to an interfund transfer of equity or to the closing of revenue and expenditure accounts at the end of the year. It is suggested that the director of the accounting department be the only person who can approve entries to an equity account.

Electronic Data Processing Division (EDP)

Our review of EDP indicated that overall controls and operating efficiency are generally adequate.

Recommendations:

- o Organize a management steering committee to establish policy, evaluate progress, and discuss division problems. The committee should consist of the EDP executive, the manager, and other key Department of Highways executives who's divisions use data processing reports. Minutes of committee meetings should be kept.
- o In conjunction with the accounting division, establish special training programs for presentation to users of EDP reports. The programs should be updated on a routine basis. Material in the training programs should not be limited to, but should include:
 - . Description and sample of all reports available
 - . Frequency schedule of times reports are prepared and available

- Deadline dates for entering data into the reports
- Personnel responsible for various reports
- Relationship of reports to each other
- Suggested filing system for reports
- Suggested length of time to keep the reports on hand

Allowance for Possible Doubtful Accounts Receivable

At June 30, 1976, the Department's total accounts receivable amounted to \$689,022. Many of these receivables were due from nongovernmental units--insurance companies, contractors, individuals, etc. Like a commercial enterprise, the Department does experience a certain amount of bad debt losses from receivables. No provision has been made for such losses.

Recommendation: An allowance for possible doubtful accounts should be established. To do this, individual accounts receivable should be carefully reviewed at least quarterly. The results of this review, together with historical bad debt trends of the Department, should be used as a basis for determining the probable loss from recorded accounts receivable.

Costs to Be Allocated to Projects or Other Departments

Certain costs of the Earmarked Revenue Fund, the Motor Pool Fund and the Equipment Bureau Fund are accumulated and considered in determining charges to projects or other state departments for use of vehicles and equipment. Unreimbursed costs, or reimbursements in excess of costs are recorded as an asset or a liability by the Department. Generally accepted accounting principles require that these unreimbursed costs or reimbursements in excess of costs be recognized as expenditures or revenues of the fiscal period in which they occur. At June 30, 1976, total unreimbursed costs of this nature amounted to \$37,178, and reimbursements in excess of costs amounted to \$536,184.

Recommendation: Unreimbursed costs and reimbursements in excess of costs to be allocated to projects or other departments should be recognized as expenditures or revenues in the proper fiscal period. This does not conflict with the Department's overall objective of using these amounts in establishing and/or adjusting billing rates for use of vehicles and equipment.

Unreimbursed Costs for Construction Work in Disaster Areas

These costs are capitalized as incurred. They are carried as an asset until such time that (1) the amount of reimbursement from the federal or other governmental units is determined, (2) the amount is determined to be a capital asset, or (3) the amount is determined to be an expenditure. Disposition of these costs does not always appear to be made on a timely basis. Unreimbursed costs at June 30 of each year are as follows:

1974	\$ -0-
1975	151,049
1976	519,466

Recommendation: Unreimbursed costs for construction work in disaster areas should be carefully monitored to determine the final disposition of costs incurred. This may necessitate a quarterly listing of costs, by project, and a written status report by the person responsible for the project.

State Highway Building Construction Project

For internal purposes, the Department is accounting for costs and debt related to the construction of a new Department of Highways building complex. The state has issued general obligation bonds to finance the project. The Department does not have responsibility to account for either the project or the related financial arrangements. Such accounting is the responsibility of other state accounting funds. Amounts included in the Earmarked Revenue Fund financial statements at June 30, 1976 are as follows:

Assets:

Proceeds receivable from highway building fund bonds	\$7,381,737
Funds segregated for highway building sinking fund	323,316
Authorized construction in progress	27,026
Property, plant and equipment--buildings	764,691
Liability--state general obligation bonds payable	7,400,000
Revenues--interest earned on highway building fund bond proceeds	48,862
Expenditures--interest expense on highway building fund bonds	25,546

Recommendation: Account balances related to the new building complex should, after coordination with other appropriate state officials, be removed from the Earmarked Revenue Fund of the Department. The Department may desire to maintain a memorandum record of these amounts for management information purposes.

Property, Plant and Equipment

Generally accepted accounting principles require that a separate General Fixed Assets group of accounts be established to account for property, plant and equipment (fixed assets) except for those accounted for in the Motor Pool Fund and the Equipment Bureau Fund. A well-managed general fixed assets group of accounts provides four kinds of information. It (1) establishes a record of fixed assets, (2) identifies their financing source(s), (3) fixes the responsibility for the custody and use of particular assets, and (4) provides valuable managerial information. Pinpointing the responsibility for individual assets is important because fixed assets are costly and valuable investments. Good records contain data on prices, suppliers, maintenance costs, and useful life. The Department has substantially complied with all of these items except for the establishment of this group of accounts in a manner that they not be accounted for within the Earmarked Revenue Fund of the Department.

Recommendation: The Department should as soon as possible, and with proper approval of appropriate state officials, establish

separate accounts to account for the fixed assets currently being accounted for in its Earmarked Revenue Fund.

Inventory Receipts and Claims Payable

Under the present system of accounting, each receiving location has a receiving stamp for use in indicating the person receiving the goods and the date the goods were received. We found this stamp was not always properly used. In many instances, the date of recorded receipt was the date the coding sheet was sent to the Department's accounting office. The present system makes it difficult to ensure that all goods received were included in inventory (or expenditures) and claims payable in the proper accounting period.

Recommendation: Receiving logs with columns for goods received, quantity, vendor name, date, and the person's name who received the goods, should be prepared at each receiving location. The logs, together with appropriate invoices would be sent to the accounting department for processing. These procedures would help ensure that all goods received were placed in Highway Department inventory (or expenditures), and can be used to determine whether claims payable are recorded in the proper accounting period.

Federal and Private Revenue Fund Accounting

Revenues and expenditures of the Federal and Private Revenue Fund are accumulated by project, cumulatively. The accounting system is not designed for accumulation of revenues and expenditures on a monthly and annual basis. Reports are prepared (monthly and annually) which require presentation of revenues and expenditures since the beginning of the fiscal year. Preparation of these reports require that revenues and expenditures be accumulated separately rather than being able to readily obtain the information from the general ledger.

Recommendation: The Department's accounting system should be designed to show revenues and expenditures, by type, accumulated between the beginning of a fiscal year and the date reports are prepared.

Retirees' Health Insurance Fund

The Department acts in a fiduciary capacity in accepting payments from qualifying retirees for continuance of their group health insurance. We found that the individual retiree ledger cards were not reconciled to the general ledger. Additionally, insurance applications were not on hand for all employees covered under the retirement plan. And applications that were on hand were not arranged in an orderly manner.

Recommendation: The detail ledger showing individual insurance payments made in advance by the retirees should be reconciled to the general ledger on a monthly basis. A file should be kept containing current applications in alphabetical order for each retiree.

City and County Construction Fund

At June 30, 1975, the details of amounts held for cities and counties did not reconcile to the fund balance. This situation was corrected during the year ended June 30, 1976.

Recommendation: Details of this fund, by city and county, should be reconciled to the general ledger on a continuing basis, preferably monthly.

Gross Vehicle Weight Division Collections

Among other things, this division of the Department is responsible for the collection of certain vehicle weight fees, combine permits, advalorem taxes, etc. The accounting for these collections is recorded in the Highway Agency Account Fund. As a general rule, most collections are distributed

to the Department's Earmarked Revenue Fund and to other appropriate governmental units during the month following collection. The delayed distribution is necessitated because of the time required to make proper allocations in accordance with appropriate laws. During the course of our work we noted that the distribution of some collections is, however, delayed for unusually long periods of time. For example, license plate charges of \$14,906 collected since July of 1973 and custom combine permit charges of \$31,110 collected in September of 1975 had not been distributed as of June 30, 1976. Additionally, most other collection categories in the Highway Agency Account Fund show minor carryover balances which have accumulated and not been distributed on a timely basis.

Recommendations:

1. Distribution of all collections on a timely basis will give the Department's Earmarked Revenue Fund and other governmental units a more timely picture of revenue trends. Reference should be made to the comment entitled Backlog of Computer Input Data.
2. The Earmarked Revenue Fund, based on revenue trends developed from its timely receipt of Highway Agency Account Fund distributions, should institute the policy of accruing this revenue in accordance with generally accepted accounting procedures.

Backlog of Computer Input Data

The Gross Vehicle Weight Division (GVW) of the Department had at June 30, 1976, a significant backlog of work waiting to be keypunched. This backlog has delayed the reconciliation of county collections, of fee permits, and other items for extended periods of time. For example, total county collections had not been reconciled for over a year.

Recommendation: GVW should consider having its own keypunch operator rather than having to wait for available time from the data

processing department. This recommendation also relates to a recommendation under the comment entitled GVW Collections.

Special Fuel Permit Fines

As collected, these fines are sent to the Gross Vehicle Weight Division (GVW) of the Highway Department. The Division then forwards the money to the Highway Department accounting office. This causes unnecessary handling of cash and increases the possibility of loss and delays in deposit.

Recommendation: Collections should be sent directly to the Highway Department accounting office. A copy of the report would also be sent to the GVW division.

Unused Permit Tickets of the Gross Vehicle Weight Division (GVW)

Unused permit tickets returned from weigh stations are kept in an unlocked warehouse adjoining the GVW headquarters in Helena. The tickets are currently uncontrolled as to access by some employees. Such employees also have the responsibility to issue tickets.

Recommendation: The unused tickets, after being rechecked against the listing of tickets returned, should be more carefully controlled, if not destroyed. This procedure will provide better internal control over the possibility of misuse of tickets.

Accrued Payroll

At June 30, 1976, the accrued payroll and payroll benefits of the Department were inadvertently recorded by showing a reduction in cash rather than a liability for the amount due employees. While the payroll expenditure was recorded in the proper accounting period, the accounting procedure followed did not properly disclose assets and liabilities. Amounts involved are disclosed in Note K to the financial statements and are as follows:

Earmarked Revenue Fund	\$386,248
Federal and Private Revenue Fund	525,691
Motor Pool Fund	2,963
Equipment Bureau Fund	57,131

Recommendation: Future payroll accruals should be properly recorded as an accrued liability. This procedure is especially important at year end.

Emergency Sick Leave

Section 1-0304.89 of the Montana Administrative Manual states that sick leave records must distinguish between emergency sick leave and regular sick leave. Emergency sick leave is charged against the employee's sick leave credits, but may not exceed five work days per calendar year. Without adequate records that distinguish between emergency and regular sick leave, it is difficult to determine the extent of compliance with appropriate regulations.

Recommendation: The record system for reporting sick leave should be adjusted to provide information regarding both emergency and regular sick leave.

Payroll Checks

Good internal control over cash disbursements requires that the person initiating disbursement information not have access to the actual disbursement. Presently, though all payroll checks are written in Helena, the completed payroll checks are returned to the payroll clerk in the division offices. This person has access to both the check and to the accounting records supporting that disbursement.

Recommendation: The completed payroll checks and payroll journal should be returned from the accounting bureau in Helena to the division manager. The journal could then be returned to the payroll clerk for review. The checks, however, should

be distributed by the division manager or another designated employee, but not the payroll clerk or any other employee associated with the hiring process or with the handling of originating payroll records.

Employee W-2 Forms

Each year a number of W-2 forms are returned for lack of complete addresses. The returned forms are investigated and followed up by employees of the payroll department.

Recommendation: Returned W-2 forms should be investigated and followed up by employees other than from the payroll department.

Ernst & Ernst

850 Lincoln Building • W 818 Riverside Avenue • Spokane, WA 99201 • Phone 509/838-2561

The Legislative Audit Committee of the Montana State Legislature

We have examined the financial statements of the various funds of the Department of Highways of the State of Montana for the years ended June 30, 1976 and June 30, 1975, as listed in the accompanying table of contents. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Earmarked Revenue Fund

For reasons described in Note C to financial statements, the accompanying statement of revenues and expenditures of the Earmarked Revenue Fund does not include a comparison with a formal budget, as required by generally accepted accounting principles.

The Department, as described in Note B to financial statements, does not provide for possible losses on doubtful accounts receivable. However, experience has shown that the Earmarked Revenue Fund traditionally experiences bad debts arising from accounts receivable.

As described in Note B to financial statements, Earmarked Revenue Fund collections from the Highway Agency Account Fund are recorded as revenue at time of receipt. Undistributed collections are susceptible to accrual by the Earmarked Revenue Fund and therefore should be accrued in accordance with generally accepted accounting principles.



Certain unreimbursed overhead costs, and reimbursements in excess of such costs are accounted for as an asset or a liability, respectively, as described in Note B to financial statements. Unreimbursed costs at June 30, 1974 in the amount of \$1,287,803 were so included as an asset in the financial statements as of that date prepared by the Department. These costs were subsequently included with assets transferred to the Equipment Bureau Fund and, as disclosed in the statement of changes in equity for the year ended June 30, 1975, were subsequently charged against equity of the Equipment Bureau Fund. Additionally, there were similar unreimbursed overhead costs or reimbursements in excess of costs at June 30, 1975 and 1976. In order to conform with generally accepted accounting principles, unreimbursed overhead costs and reimbursements in excess of such costs should have been recognized as either expenditures or revenues, respectively, in the fiscal year in which they occurred.

The Department includes certain transactions in its Earmarked Revenue Fund, as described in Note E to financial statements, which are duplicative of amounts reportable in other state accounting funds. Therefore, the reporting of such amounts in the Earmarked Revenue Fund is not in accordance with generally accepted accounting principles. Further, as to \$300,000 of the amount segregated for highway building sinking fund, such amount should have been recorded as an expenditure in the year ended June 30, 1976, together with a corresponding liability to the State Debt Service Fund.

As described in Note B to financial statements, authorized construction in progress is recorded as an asset until such time projects are completed, at which time the costs are transferred to either property, plant and equipment accounts or expenditure accounts. However, in order to conform with generally accepted accounting principles, the costs should be recorded as expenditures, and appropriate assets should be accounted for in a separate general fixed assets group of accounts which should be excluded from the Earmarked Revenue Fund.

The Department also includes property, plant and equipment accounts in its Earmarked Revenue Fund. Some of these amounts have resulted from Earmarked Revenue Fund expenditures. Other amounts have resulted from recognizing assets used by or under the control of the Department, which were paid for by other state departments or governmental entities. However, in order to be in conformity with generally accepted accounting principles, the cost of assets purchased through the Earmarked Revenue Fund should be recorded as expenditures rather than as property, plant and equipment; and all such property, plant and equipment should be accounted for in a separate general fixed assets group of accounts separate and apart from the Earmarked Revenue Fund.

At June 30, 1976, the cost of equipment purchased for \$177,444 and a corresponding liability for that amount had not been recorded in the accounts of the Earmarked Revenue Fund.

As of June 30, 1976, accrued payroll and payroll benefits of \$386,248 were not classified as a part of "claims payable and accrued expenses", but were classified as a reduction of "equity in State Treasurer's funds". As a result, the amounts shown for each of these two classifications in the balance sheet are understated by \$386,248 at June 30, 1976.

As described in Note F to financial statements, there was a duplicate expenditure transfer of \$531,078 from the Earmarked Revenue Fund to the Federal and Private Revenue Fund for the State's share of highway construction costs in the year ended June 30, 1976.

In our opinion, because of the effects of the matters discussed in the preceding paragraphs, the accompanying financial statements of the Earmarked Revenue Fund do not present fairly, in conformity with generally accepted accounting principles, the financial position of the Earmarked Revenue Fund as of June 30, 1976 or June 30, 1975, or the results of its operations for the years then ended.

As described in Note J to financial statements, there is substantial contingent liability as a result of lawsuits, the ultimate outcome of which cannot presently be determined. Furthermore, the manner of funding an award of \$1,327,271 to a contractor has not yet been determined. No provision for any liability that may result from these matters has been made in the Earmarked Revenue Fund financial statements, and thus they are subject to the effects of adjustments depending upon the outcome of such matters.

Special Revenue Funds

For reasons described in Note C to financial statements, the accompanying statements of revenues and expenditures of the Federal and Private Revenue Fund and the Coal Area Highway Improvement Fund do not include a comparison with a formal budget, as required by generally accepted accounting principles.

As of June 30, 1976, \$4,701,442 of federal aid revenue which was due from the federal government was classified in the balance sheet of the Federal and Private Revenue Fund as a part of "equity in State Treasurer's funds". This amount should have been classified as an account receivable because the cash funds were not received until July 2, 1976. Furthermore, all federal aid revenue of the Federal and Private Revenue Fund is normally recorded as revenue at the time of receipt, as described in Note D to financial statements. Federal aid revenue is susceptible to accrual, and therefore should be accrued in accordance with generally accepted accounting principles.

As of June 30, 1976, Federal and Private Revenue Fund accrued payroll and payroll benefits of \$525,691 were not classified as a part of "claims payable and accrued expenses", but were classified as a reduction of "equity in State Treasurer's funds". As a result, the amounts shown for each of these two classifications in the Balance Sheet are understated by \$525,691 at June 30, 1976.

As described in Note F to financial statements, a duplicate state aid revenue transfer of \$531,078 was received by the Federal and Private Revenue Fund from the Earmarked Revenue Fund in the year ended June 30, 1976.

In our opinion, because of the effects of the matters discussed in the preceding paragraphs, the accompanying financial statements of the Federal and Private Revenue Fund do not present fairly, in conformity with generally accepted accounting principles, the financial position of the Federal and Private Revenue Fund as of June 30, 1976 or June 30, 1975, or the results of its operations for the years then ended.

Furthermore, in our opinion, except for the omission of budget information, the accompanying financial statements of the Coal Area Highway Improvement Fund present fairly the financial position of the Coal Area Highway Improvement Fund at June 30, 1976, and the results of its operations for the year then ended, in conformity with generally accepted accounting principles.

Intragovernmental Service Funds

As described in Note B to financial statements, certain unreimbursed overhead costs and reimbursements in excess of such costs are accounted for as an asset or a liability, respectively, in the Motor Pool Fund and the Equipment Bureau Fund. Generally accepted accounting principles require that these unreimbursed overhead costs and reimbursements in excess of such costs be recognized as either expenditures or revenues, respectively, in the fiscal year in which they occur.

As described in Note G to financial statements, during 1976 the Department revised the estimated useful lives of various depreciable assets of the Equipment Bureau Fund. However, retroactive effect was given to the revision in lives which caused depreciation expense for the year to increase substantially in the Equipment Bureau Fund. In order to conform with generally accepted accounting principles, depreciation should have been charged to operations prospectively based on the remaining useful lives of the assets.

As of June 30, 1976, Equipment Bureau Fund accrued payroll and payroll benefits of \$57,131 were not classified as a part of "claims payable and accrued expenses", but were classified as a reduction of "equity in State Treasurer's funds". As a result, the amounts shown for each of these two classifications in the balance sheet of the Equipment Bureau Fund are understated by \$57,131 at June 30, 1976.

In our opinion, except for the effects on each Intragovernmental Service Fund of not recognizing expenditures and revenues as described above, and except for the effects on the Equipment Bureau Fund of recording depreciation charges retroactively and of recording accrued payroll in the manner described above, the accompanying financial statements present fairly the financial position of the intragovernmental service funds at June 30, 1976 and June 30, 1975, and the results of their operations for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Trust and Agency Funds

In our opinion, the accompanying financial statements of the trust and agency funds present fairly the financial position of the trust and agency funds at June 30, 1976 and June 30, 1975, and the cash receipts and disbursements for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

The column on the accompanying balance sheets captioned "Total (Memorandum Only)" is not necessary for a fair presentation of the balance sheets, but is presented for summary analytical purposes only.

Trust + Ernst

Spokane, Washington
October 8, 1976



FINANCIAL STATEMENTS

BALANCE SHEETS

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

June 30, 1976

	Earmarked Revenue Fund	Federal and Private Revenue	Special Revenue Funds (Note D)	Coal Area Highway Improvement
ASSETS				
Equity in State Treasurer's funds	\$17,892,561	\$13,388,290		\$2,203,181
Imprest cash funds	6,350			
Accounts receivable	629,177			
Inventories	6,117,966			
Advances to:				
Federal and Private Revenue Fund	5,403,056			
Motor Pool Fund	129,461			
Another state department for architectural and engineering services	49,147			
Unreimbursed costs for construction work in disaster areas	519,466			
Unreimbursed costs to be allocated to other state departments and divisions				
Travel advances	13,635			
Proceeds receivable from highway building fund bonds--Note E	7,381,737			
Funds segregated for highway building sinking fund--Note E	323,316			
Authorized construction in progress	187,292			
Property, plant and equipment:				
Land and buildings--Note E	14,005,476			
Furniture, fixtures and tools	2,094,182			
Equipment	2,552,158			
Allowances for depre- ciation (deduction)	<u>(1,136,967)</u>			
	<u>\$56,168,013</u>	<u>\$13,388,290</u>		<u>\$2,203,181</u>

See notes to financial statements

Intragovernmental Service Funds		Trust and Agency Funds					Total (Memorandum Only)
Motor Pool	Equipment Bureau	Highway Agency Account	City and County Construction	Retirees' Health Insurance	Outdoor Sign Control		
\$342,645	\$ 765,030	\$622,911	\$1,443,872	\$4,493		\$36,662,983	6,350
37,654	21,650		541			689,022	
7,200	635,619					6,760,785	
						5,403,056	
						129,461	
						49,147	
						519,466	
2,995	34,183					37,178	
						13,635	
						7,381,737	
21,657						323,316	
						208,949	
173,600						14,179,076	
11,031	303,604					2,408,817	
656,141	14,587,032					17,795,331	
(244,599)	(6,656,366)	_____	_____	_____	_____	(8,037,932)	
\$986,667	\$ 9,712,409	\$623,452	\$1,443,872	\$4,493	\$-0-	\$84,530,377	
<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>

BALANCE SHEETS (Continued)

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

June 30, 1976

	Earmarked Revenue Fund	Special Revenue Funds	
		Federal and Private Revenue	Coal Area Highway Improvement
LIABILITIES, RESERVES AND EQUITY			
Claims payable and accrued expenses	\$ 428,324	\$ 472,192	
Distributable to Montana counties and state departments			
Amounts designated for city and county road construction and repair			
Retiree payments designated for future health insurance premiums			
Reimbursements from other state departments in excess of costs	536,184		
Advances from Earmarked Revenue Fund		5,403,056	
Reserve for completion of con- struction projects--Note F		7,513,042	
State general obligation bonds--Note E	7,400,000		
Equity:			
Contributions from other funds			
Retained earnings			
Fund balance	47,803,505		\$2,203,181
Total equity	47,803,505		2,203,181
	<u>\$56,168,013</u>	<u>\$13,388,290</u>	<u>\$2,203,181</u>

See notes to financial statements

<u>Intragovernmental Service Funds</u>		<u>Trust and Agency Funds</u>					Total (Memorandum Only)
Motor Pool	Equipment Bureau	Highway Agency Account	City and County Construction	Retirees' Health Insurance	Outdoor Sign Control		
\$ 11,275	\$ 388,015					\$ 1,299,806	
		\$623,452				623,452	
			\$1,440,349			1,440,349	
				\$4,493		4,493	
129,461			3,523			536,184 5,536,040	
						7,513,042	
						7,400,000	
773,233	8,496,479					9,269,712	
72,698	827,915					900,613	
<u>845,931</u>	<u>9,324,394</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>50,006,686</u>	
<u>\$986,667</u>	<u>\$9,712,409</u>	<u>\$623,452</u>	<u>\$1,443,872</u>	<u>\$4,493</u>	<u>\$-0-</u>	<u>60,177,011</u>	
						<u>\$84,530,377</u>	

BALANCE SHEETS

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

June 30, 1975

	Earmarked Revenue Fund	Special Revenue Fund Federal and Private Revenue (Note D)
ASSETS		
Equity in State Treasurer's funds	\$17,253,317	\$7,309,419
Imprest cash funds	6,450	
Accounts receivable	471,643	
Inventories	5,737,653	
Advances to:		
Federal and Private Revenue Fund	9,724,976	
Motor Pool Fund	103,595	
Equipment Bureau Fund	659	
Another state department for architectural and engineering services	135,660	
Unreimbursed costs for construction work in disaster areas	151,049	
Unreimbursed costs to be allocated to other state departments and divisions	151,502	
Travel advances	10,433	
Authorized construction in progress	178,184	
Property, plant and equipment:		
Land and buildings--Note E	13,338,462	
Furniture, fixtures and tools	2,081,780	
Equipment	2,419,418	
Allowances for depre- ciation (deduction)	<u>(1,127,166)</u>	
	\$50,637,615	\$7,309,419

See notes to financial statements

Intragovernmental Service Funds		Trust and Agency Funds					Total (Memorandum Only)
Motor Pool	Equipment Bureau	Highway Agency Account	City and County Construction	Retirees' Health Insurance	Outdoor Sign Control		
\$248,031	\$ 1,583,929	\$258,952	\$2,167,457	\$2,208			\$28,823,313
94,235	25,420						6,450
	676,902						591,298
							6,414,555
							9,724,976
							103,595
							659
							135,660
							151,049
6,489							157,991
	12,927						10,433
127,635							191,111
11,851	296,056						13,466,097
602,388	13,904,471						2,389,687
(119,745)	(6,138,006)	_____	_____	_____	_____	_____	16,926,277
\$970,884	\$10,361,699	\$258,952	\$2,167,457	\$2,208	\$-0-		(\$71,708,234)

BALANCE SHEETS (Continued)

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

June 30, 1975

		<u>Special Revenue Fund</u>
	Earmarked Revenue Fund	Federal and Private Revenue (Note D)
LIABILITIES, RESERVES AND EQUITY		
Claims payable and accrued expenses	\$ 2,869,791	\$ 817,964
Distributable to Montana counties and state departments		
Amounts designated for city and county road construction and repair	.	
Retiree payments designated for future health insurance premiums		
Reimbursements from other state departments in excess of costs	570,566	
Advances from Earmarked Revenue Fund		9,724,976
Reserve (deficiency) for completion of construction projects		(3,233,521)
Equity:		
Contributions from other funds		
Retained earnings	<u>47,197,258</u>	<u>47,197,258</u>
Fund balance		
Total equity	<u>\$50,637,615</u>	<u>\$7,309,419</u>

See notes to financial statements

<u>Intragovernmental Service Funds</u>		<u>Trust and Agency Funds</u>					Total (Memorandum Only)
Motor Pool	Equipment Bureau	Highway Agency Account	City and County Construction	Retirees' Health Insurance	Outdoor Sign Control		
\$ 14,958	\$ 1,033,294		\$ 1,267				\$ 4,737,274
		\$258,952					258,952
			2,166,190				2,166,190
				\$2,208			2,208
103,595	16,037 659						586,603 9,829,230
							(3,233,521)
795,312 57,019	8,178,671 1,133,038						8,973,983 1,190,057 47,197,258 57,361,298
<u>852,331</u>	<u>9,311,709</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>
<u>\$970,884</u>	<u>\$10,361,699</u>	<u>\$258,952</u>	<u>\$2,167,457</u>	<u>\$2,208</u>	<u>\$-0-</u>	<u>_____</u>	<u>\$71,708,234</u>

STATEMENTS OF CHANGES IN EQUITY

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

Year Ended June 30, 1976

	Earmarked Revenue Fund	Special Revenue Fund Coal Area Highway Improvement	Intragovernmental Service Funds Motor Pool	Equipment Bureau
Equity July 1, 1975	\$47,197,258	\$ -0-	\$852,331	\$9,311,709
Additions (deductions):				
Reduction of amounts due from other state depart- ments at beginning of year			(22,079)	
Appraisal value of land owned but not previously recorded in financial statements		483,955		
Adjustment of allowance for depreciation transferred from Earmarked Revenue Fund in 1975				170,113
To write off pension trust costs of prior years included in unreimbursed costs to be allocated to other departments		(78,568)		
Transfers to Equipment Bureau		(87,695)		87,695
Elimination of allowance for depreciation accounts relating to nonrevenue producing assets no longer being depreciated		147,445		
Federal share of equipment additions		15,180		
Donation from Department of Intergovernmental Relations				60,000
Excess (deficiency) of revenues over expenditures and transfers	97,078	2,203,181	15,679	(310,245)
Miscellaneous adjustments	<u>28,852</u>	<u>_____</u>	<u>_____</u>	<u>5,122</u>
Equity June 30, 1976	<u>\$47,803,505</u>	<u>\$2,203,181</u>	<u>\$845,931</u>	<u>\$9,324,394</u>

See notes to financial statements

STATEMENTS OF CHANGES IN EQUITY

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

Year Ended June 30, 1975

	Earmarked Revenue Fund	Intragovernmental Service Funds	
		Motor Pool	Equipment Bureau
Equity July 1, 1974		\$53,235,290	\$939,697
Additions (deductions):			
Unreimbursed costs as of July 1, 1974 for prior construction work in disaster areas		74,965	
Transfers of assets from Earmarked Revenue Fund in order to form Equipment Bureau Fund		(9,466,474)	9,466,474
Elimination of unreimbursed costs transferred from Earmarked Revenue Fund			(1,287,803)
Transfers of equipment from Motor Pool Fund		144,385	(144,385)
Elimination of allowance for depreciation accounts relating to nonrevenue producing assets no longer being depreciated		708,617	
Federal share of rest area construction costs added to property and equipment		2,106,667	
Excess of revenues over expenditures and transfers		401,328	56,820
Miscellaneous adjustments	<u>(7,520)</u>	<u>199</u>	<u>3,190</u>
Equity June 30, 1975		<u>\$47,197,258</u>	<u>\$852,331</u>
			<u>\$9,311,709</u>

See notes to financial statements

STATEMENT OF REVENUES AND EXPENDITURES--EARMARKED REVENUE FUND

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

Years Ended June 30

	1976	1975
Revenues:		
Motor fuel taxes	\$41,175,759	\$36,302,171
U.S. Government permits	2,243,054	2,384,922
Gross vehicle weight taxes	11,383,710	9,875,305
Gross vehicle weight licenses	157,756	266,607
Vehicle excess size and weight taxes	304,950	236,359
Restricted route load permits	180,870	123,390
Interest earned on highway building fund bond proceeds--Note E	48,862	
Handling charges and miscellaneous	<u>138,974</u>	<u>72,350</u>
	<u>55,633,935</u>	<u>49,261,104</u>
Expenditures:		
General administration	2,137,301	2,088,143
Field division engineering administration	746,797	681,273
Maintenance supervision and overhead	1,671,362	1,603,139
Maintenance	15,571,481	14,587,759
Motor fuel and road oil storage facility repairs	27,863	27,231
Incidental land expense	15,545	
Communications expense	196,757	236,522
Building repairs	174,308	176,663
Equipment repairs	32,292	68,215
Gross vehicle weight tax collection expense	1,270,980	1,051,625
Convention and tour expense		24,996
Travel promotion expense	656,989	753,507
Bad debts	7,023	5,227
Fixed cost charges for unused mobile equipment	298,616	388,746
Repairs to roadside rest areas	359,565	271,591
Depreciation--nonvehicle and related equipment	76,671	39,455
Construction engineering administration	295,316	239,814
Right-of-way administration	646,653	678,143
Preliminary engineering administration	689,847	670,160
Interest expense on highway building fund bonds--Note E	25,546	
Inventory adjustment (credit)	(38,612)	(24,070)
Prior year expenditure adjustment (credit)	(277)	(1,184)
Transfers:		
Legislative appropriation--motor fuel taxes distributed to other state departments and governmental units	10,075,318	6,080,286
To Federal and Private Revenue Fund for state share of highway construction costs--Note F	<u>20,599,516</u>	<u>19,212,535</u>
	<u>55,536,857</u>	<u>48,859,776</u>
Excess of revenues over expenditures and transfers	<u>\$ 97,078</u>	<u>\$ 401,328</u>

See notes to financial statements

STATEMENT OF REVENUES AND EXPENDITURES--SPECIAL REVENUE FUNDS

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

Year Ended June 30

	<u>Federal and Private Revenue</u>	<u>Coal Area Highway Improvement</u>
	1976	1975
	(Note D)	(Note D)
Revenues:		
Severance tax		\$2,203,181
State aid	\$20,599,516	\$19,212,535
Federal aid	77,142,628	47,749,616
Miscellaneous receipts	242,354	195,506
Change in reserve for completion of construction projects (deduction)	<u>(10,746,563)</u>	<u>(6,006,169)</u>
	<u>87,237,935</u>	<u>61,151,488</u>
		<u>2,203,181</u>
Expenditures:		
Preliminary engineering	3,779,311	3,409,644
Right of way	3,629,140	3,695,601
Utility relocation	1,193,343	1,762,961
Construction supervision	8,185,396	6,762,299
Construction contracts	69,037,725	44,080,190
Administrative settlement costs	78,259	11,327
Planning and research	1,302,137	1,246,215
Control of outdoor advertising	<u>32,624</u>	<u>183,251</u>
	<u>87,237,935</u>	<u>61,151,488</u>
Excess of revenues over expenditures	<u>\$ -0-</u>	<u>\$ -0-</u>
		<u>\$2,203,181</u>

Note: The coal area highway improvement fund was formed during the year 1976.

See notes to financial statements



STATEMENT OF REVENUES AND EXPENDITURES--INTRAGOVERNMENTAL SERVICE FUNDS

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

Years Ended June 30

	Motor Pool		Equipment Bureau	
	1976	1975	1976	1975
Revenues:				
Billings to other highway department operations and other state departments	\$454,420	\$481,069	\$4,694,316	\$5,173,932
Handling charges and miscellaneous	<u>926</u>	<u>18,957</u>	<u>14,629</u>	<u>6,763</u>
	<u>455,346</u>	<u>500,026</u>	<u>4,708,945</u>	<u>5,180,695</u>
Expenditures:				
Labor	73,438	90,288	1,429,347	1,297,698
Labor overhead	22,480	29,540	379,464	432,516
Insurance	20,466	14,711	70,983	46,297
Rents and utilities	11,128	27,235	53,482	55,840
Repairs and services	8,626	8,253	25,282	20,434
Maintenance materials	6,049	7,184	287,853	243,928
Repair, parts, supplies and accessories	157,618	156,309	1,753,753	1,431,531
Equipment rental	470	2,723	71,980	79,590
Depreciation--Note G	132,631	100,909	803,960	346,873
Other	<u>6,761</u>	<u>6,054</u>	<u>143,086</u>	<u>96,140</u>
	<u>439,667</u>	<u>443,206</u>	<u>5,019,190</u>	<u>4,050,847</u>
Excess (deficiency) of revenues over expenses	<u>\$ 15,679</u>	<u>\$ 56,820</u>	<u>\$ (310,245)</u>	<u>\$1,129,848</u>

See notes to financial statements

STATEMENTS OF CASH RECEIPTS AND DISBURSEMENTS--TRUST AND AGENCY FUNDS

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

Year Ended June 30

	<u>Highway</u>	<u>Agency</u>	<u>Account</u>
	1976	1975	
Equity in State Treasurer's funds	\$ 258,952	\$ 130,300	
 Receipts:			
Gross vehicle weight fees, combine permits, custom combine vehicle permits, and advalorem taxes	2,062,035	1,738,859	
Retiree remittances			
Premium adjustment from insurance carrier			
Outdoor advertising sign permits			
	<u>Total Receipts</u>	<u>2,062,035</u>	<u>1,738,859</u>
	<u>Total Funds Available</u>	<u>2,320,987</u>	<u>1,869,159</u>
 Disbursements:			
Distributions to Montana counties and state departments arising from:			
Gross vehicle weight fees	77,061	70,347	
Combine permits	38,090	26,775	
Custom combine vehicle permits	30,575	21,275	
Advalorem taxes	1,552,350	1,491,810	
City and county construction			
Health insurance premiums			
Premium adjustments to retirees			
Distribution to Earmarked Revenue Fund			
	<u>Total Disbursements</u>	<u>1,698,076</u>	<u>1,610,207</u>
Equity in State Treasurer's funds	\$ 622,911	\$ 258,952	

See notes to financial statements

City and County Construction		Retirees' Health Insurance		Outdoor Sign Control	
1976	1975	1976	1975	1976	1975
\$2,167,457	\$4,103,986	\$ 2,208	\$ 3,409	\$ -0-	\$ 699
		60,001	34,343		
		25,502			
		<u>85,503</u>	<u>34,343</u>	<u>8,079</u>	<u>2,698</u>
		<u>87,711</u>	<u>37,752</u>	<u>8,079</u>	<u>2,698</u>
				<u>8,079</u>	<u>3,397</u>
<u>2,167,457</u>	<u>4,103,986</u>				
723,585	1,936,529	57,716	35,544		
		25,502			
<u>723,585</u>	<u>1,936,529</u>	<u>83,218</u>	<u>35,544</u>	<u>8,079</u>	<u>3,397</u>
<u>§1,443,872</u>	<u>§2,167,457</u>	<u>\$ 4,493</u>	<u>\$ 2,208</u>	<u>\$ -0-</u>	<u>\$ -0-</u>

NOTES TO FINANCIAL STATEMENTS

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

NOTE A--DESCRIPTION OF FUNDS

Operations of the Department of Highways of the State of Montana (Department) are accounted for in the various funds which are described below and classified by general purpose.

Earmarked Revenue Fund: This fund, which is the "General Fund" of the Department, has been created to account for all financial transactions not accounted for in any other fund. This fund is therefore used to account for nearly all current and routine operations of the Department.

Special Revenue Funds: Special revenue funds have been created to account for revenues which must be used to finance a particular function or specific activities in accordance with legal or administrative requirements. Special revenue funds are as follows:

Federal and Private Revenue Fund: To account for receipt and expenditure of federal and state monies designated for highway construction projects.

Coal Area Highway Improvement Fund: To account for receipt and expenditure of coal taxes allocated for the improvement of deficient highway sections in the eastern Montana coal field economic growth center.

Intragovernmental Service Funds: Intragovernmental service funds have been created for special activities and/or services which are performed for other highway department operations and other state departments. Intragovernmental service funds are as follows:

Motor Pool Fund: To account for the financial activities of the motor pool. Motor pool vehicles are available for use by other state departments, generally within the capitol complex area. Rental schedules have been established for use of the vehicles.

Equipment Bureau Fund: To account for the financial activities of the equipment bureau. Equipment bureau vehicles and equipment are available for use within the Department. Rental schedules have been established for use of the vehicles and equipment for appropriate projects or administrative activities.

Trust and Agency Funds: Trust and agency funds have been created for assets (principally cash collected) held under trust or agency relationships for governmental units within the State of Montana, or for individuals. Trust and agency funds are as follows:

NOTES TO FINANCIAL STATEMENTS (Continued)

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

NOTE A--DESCRIPTION OF FUNDS (Continued)

Highway Agency Account Fund: To account for various vehicle weight, permit and license fees collected by the Gross Vehicle Weight Division of the Department. Such fees are held until proper distribution can be made to appropriate counties and state departments.

City and County Construction Fund: To account for pre-July 1, 1974 gasoline, diesel fuel and liquid petroleum gas taxes allocated by the State of Montana to counties, cities and towns for authorized construction, reconstruction, maintenance and repair of roads, streets and highways.

Retirees' Health Insurance Fund: To account for payments made by qualifying retirees for continuance of their group health insurance coverage. Retirees must make the full monthly premium payment in advance. No state contribution can be made for the retiree. Retiree payments are forwarded by the Department to appropriate insurance carriers as premiums become due.

Outdoor Sign Control Fund: To account for fees received from sale of outdoor advertising permits. Such fees are transmitted to the Earmarked Revenue Fund.

NOTE B--SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting: The accrual basis of accounting is followed by the Intragovernmental Service Funds. A modified accrual basis of accounting is followed by the Earmarked Revenue Fund, which generally provides for recording revenues (other than for services provided and work performed) on the cash basis, including undistributed collections to be received from the Highway Agency Account Fund, and expenditures on the accrual basis. Special Revenue Fund and Trust and Agency Fund financial transactions are recorded at the time cash is received or disbursed, except that Federal and Private Revenue Fund construction contract retentions are recorded on the accrual basis.

Accounts Receivable: Accounts receivable of the Earmarked Revenue Fund and Intragovernmental Service Funds are recorded currently as services are provided or work is performed. No provision is made for possible losses on doubtful accounts receivable.

NOTES TO FINANCIAL STATEMENTS (Continued)

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

NOTE B--SIGNIFICANT ACCOUNTING POLICIES (Continued)

Inventories: Inventory held by the Intragovernmental Service Funds (primarily maintenance parts) and the Earmarked Revenue Fund (primarily highway construction and maintenance materials) is priced at cost (either specific identity or average cost methods).

Unreimbursed Costs for Construction Work in Disaster Areas: These costs are accounted for as an asset until such time that their realizability is determined. To the extent that such costs are not recoverable from federal or other governmental sources they are included as an expenditure of the period in which that determination is made.

Authorized Construction in Progress: Costs related to special projects are accumulated until the projects are completed, at which time the costs are transferred to capital or expenditure accounts.

Unreimbursed Costs to be Allocated and Reimbursements

in Excess of Costs Allocated: Certain assigned overhead costs (primarily payroll and payroll benefits) are accumulated and considered in determining charges to projects and other state departments for use of Department vehicles and equipment. Billings for such overhead costs are offset against costs accumulated. Excess costs or reimbursements are accounted for as an asset or liability, respectively, and are periodically considered in establishing future billing rates.

Property, Plant and Equipment: Such assets purchased are capitalized at cost. Contributed assets are capitalized at fair value at the time received. A separate general fixed asset fund is not maintained for Earmarked Revenue Fund property, plant and equipment. Depreciation is provided for using the straight-line and unit-of-production methods for revenue-producing assets (those assets for which use charges can be made to projects or other state departments). Depreciation on nonrevenue-producing assets is not provided for. Highway construction costs and related improvements are classified as expenditures.

Claims Payable: The Department follows the policy of accruing an appropriate liability and expenditure for materials and supplies as they are received. As required by the Statewide Budgeting and Accounting System, the Department also accrues a liability and related assets for valid equipment purchase orders and for contracts to purchase gravel inventory. Both of these types of liabilities are included in the accompanying balance sheets as "claims payable and accrued expenses".

NOTES TO FINANCIAL STATEMENTS (Continued)

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

NOTE B--SIGNIFICANT ACCOUNTING POLICIES (Continued)

Vacation and Sick Pay: Vacation and sick leave payments to employees are charged to expense at the time of payment. Each permanent employee may accumulate and carry over into a new calendar year a maximum of unused vacation not exceeding two times the vacation earned in the most recent year, and may carry over all unused sick leave. Payment for unused accumulated vacation is made in cash upon termination of employment. Payment for 25% of unused accumulated sick leave after July 1, 1971 is made in cash upon termination of employment. The amount of accumulated unused vacation and unused sick leave at June 30, 1976 and June 30, 1975, was not readily determinable.

NOTE C--COMPLIANCE WITH STATEWIDE BUDGETING AND ACCOUNTING SYSTEM

The Department maintains its own accounting system, which is separate from the statewide accounting system, in order to provide additional accounting and financial management information. The Department follows the statewide budgeting system. Such budgeting system does not result in appropriate relationships to the accompanying financial statements prepared from accounts maintained in the Department's accounting system.

NOTE D--SPECIAL REVENUE FUND ACCOUNTING

As indicated in Note B to the financial statements, the cash basis of accounting is followed by the special revenue funds. For such funds, generally accepted accounting principles require that the cash basis of accounting be modified to include accrual of revenues susceptible thereto and include accrual of expenditures. The Department's schedule and method of estimating and paying construction expenditures approximates the modified accrual basis for expenditures. However, certain revenues are recorded when received rather than accrued when earned. Had federal aid revenue (in the Federal and Private Revenue Fund) been recorded on the accrual basis, federal aid receivable would have been recorded in the amounts of \$2,234,507 and \$7,681,079 at June 30, 1976 and June 30, 1975, respectively, together with corresponding increases in the amount of reserve for completion of construction projects at those dates. Further, federal aid revenue would have decreased \$5,446,572 for the year 1976 and increased \$2,453,610 for the year 1975, together with corresponding amounts of changes in reserves for completion of construction projects during those years.

NOTE E--STATE GENERAL OBLIGATION BONDS PAYABLE AND RELATED ACCOUNTS

In April of 1976 the State of Montana sold General Obligation Highway Bonds in the amount of \$7,400,000. Proceeds from the sale are to provide funds

NOTES TO FINANCIAL STATEMENTS (Continued)

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

NOTE E--STATE GENERAL OBLIGATION BONDS PAYABLE AND RELATED ACCOUNTS (Continued)

toward construction of a new state highway building. Such bonds mature serially from 1977 to 1996 and bear interest at varying rates.

As provided for by the Statewide Budgeting and Accounting System and generally accepted accounting principles, all transactions relating to the bonds and the State Highway Building construction project are accounted for in other state accounting funds. Thus amounts recorded in the Department's Earmarked Revenue Fund represent for the most part duplicate accounts recorded for internal Highway Department purposes only. Amounts included in the accompanying Earmarked Revenue Fund financial statements are summarized as follows:

	June 30	
	1976	1975
Assets:		
Proceeds receivable from highway building fund bonds	\$7,381,737	
Funds segregated for highway building sinking fund	323,316	
Authorized construction in progress	27,026	
Property, plant and equipment--buildings	764,691	\$764,691
Liability--state general obligation bonds payable	7,400,000	
Revenues--interest earned on highway building fund bond proceeds	48,862	
Expenditures--interest expense on highway building fund bonds	25,546	

NOTE F--STATE SHARE OF HIGHWAY CONSTRUCTION COSTS

Transfers from the Earmarked Revenue Fund to the Federal and Private Revenue Fund for the State's share of construction costs (either state projects or participating federal and state projects) are normally accounted for as interfund advances until such time that a project is fully approved. At that time the State's total share of estimated construction costs is recorded as a transfer expenditure in the Earmarked Revenue Fund and as state aid revenue in the Federal and Private Revenue Fund.

Included for the year ended June 30, 1976 in the Federal and Private Revenue Fund as revenue from state aid and in the Earmarked Revenue Fund as a transfer expenditure for the State's share of highway construction costs is a duplicate amount of \$531,078. Such duplication overstates Earmarked Revenue Fund expenditures and Federal and Private Revenue Fund revenues for fiscal year 1976 by \$531,078.

NOTES TO FINANCIAL STATEMENTS (Continued)

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

NOTE G--CHANGE IN ESTIMATED LIVES OF DEPRECIABLE ASSETS

From time to time it is necessary for the Department to revise the estimated remaining useful lives of various depreciable assets. Such a revision was made during the year ended June 30, 1976 affecting the assets of the Equipment Bureau Fund. Retroactive adjustment was made for increased depreciation charges resulting from the revision of asset lives. This resulted in a significant increase in depreciation expense for the year 1976.

NOTE H--RETIREMENT PLAN

The Department participates in the Public Employees' Retirement System, a contributory plan which covers all employees. The Department's contribution to the plan was \$1,342,345 in the year ended June 30, 1976, and \$1,123,944 in the year ended June 30, 1975.

NOTE I--COMMITMENTS

The Department leases various office and other facilities throughout the state. Leases are normally entered into for periods of one year or less expiring on the next June 30, and provide for payment of taxes, insurance and maintenance by the lessors. Additionally, the Department enters into similar lease arrangements for various electronic data processing equipment and office equipment. It is expected that similar office and equipment leases will be entered into in future periods. Total rent expense for all leases for the years ended June 30, 1976 and June 30, 1975, amounted to \$276,491 and \$400,772, respectively.

NOTE J--CONTINGENCIES

No provision has been made in the accompanying financial statements for possible losses which may result from the unfavorable outcome of litigation. However, the state carries insurance for certain types of risks.

As of June 30, 1976, legal counsel was representing the State of Montana, the State Highway Commission and/or the Department in various actions. Such actions consist of tort claims totaling over \$11,000,000. In addition there were contractor claims totaling over \$3,500,000 (including one claim of \$1,400,000 as to which a subsequent trial resulted in an award of \$1,327,271). The manner in which this award will be funded has not yet been determined.

NOTES TO FINANCIAL STATEMENTS (Continued)

DEPARTMENT OF HIGHWAYS OF THE STATE OF MONTANA

NOTE K--EQUITY IN STATE TREASURER'S FUNDS

Equity in State Treasurer's funds as reported by the State Treasurer are reconciled to those reported in the accompanying financial statements as follows:

	<u>Special Revenue Funds</u>		
Earmarked Revenue Fund	Federal and Private Revenue	Coal Area Highway Improvement	
June 30, 1976:			
Reported by the State Treasurer	\$20,007,902	\$ 9,211,804	\$ 2,203,181
Additions (deductions):			
Accrued payroll and payroll benefits applied against cash	(386,248)	(525,691)	
Funds segregated for highway building sinking fund	(300,000)		
Amounts accounted for in the City and County Construction Fund	(1,443,872)		
Interfund transfer recorded by Treasurer after June 30, 1976	8,079		
Collection received by Treasurer on July 2, 1976		4,701,442	
Miscellaneous receipts (expend- itures) recorded by Treasurer after June 30, 1976	6,700	735	
Reported in financial statements	<u>\$17,892,561</u>	<u>\$13,388,290</u>	<u>\$2,203,181</u>
June 30, 1975:			
Reported by the State Treasurer	\$19,269,342	\$ 7,348,926	\$ -0-
Additions (deductions):			
Interfund transfers recorded by Treasurer after June 30, 1975	96,427		
Payroll charged by Treasurer to incorrect fund	56,995		
Amounts accounted for in the City and County Construction Fund	(2,167,457)		
Gross receipts tax collection accounted for by Department after June 30, 1975		(37,969)	
Miscellaneous receipts (expend- itures) recorded by Treasurer after June 30, 1976	(1,990)	(1,538)	
Reported in financial statements	<u>\$17,253,317</u>	<u>\$ 7,309,419</u>	<u>\$ -0-</u>

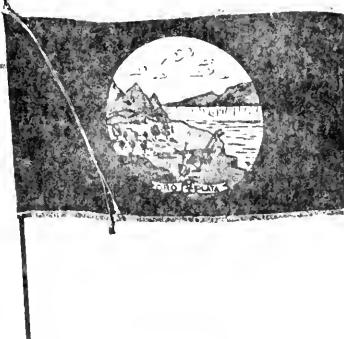
Intragovernmental Service Funds		Trust and Agency Funds				
Motor Pool	Equipment Bureau	Highway Agency Account	City and County Construction	Retirees' Health Insurance	Outdoor Sign Control	
\$347,873	\$ 826,441	\$604,864	\$ -0-	\$4,493	\$8,079	
(2,963)	(57,131)					
			1,443,872			
				(8,079)		
		17,293				
<u>(2,265)</u>	<u>(4,280)</u>	<u>754</u>				
<u>\$342,645</u>	<u>\$ 765,030</u>	<u>\$622,911</u>	<u>\$1,443,872</u>	<u>\$4,493</u>	<u>\$ -0-</u>	
\$357,640	\$1,626,440	\$258,952	\$ -0-	\$2,208	\$3,397	
(89,028)	(4,002)			(3,397)		
(56,995)						
		2,167,457				

<u>(20,637)</u>	<u>18,486</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>	<u>_____</u>
<u>\$248,031</u>	<u>\$1,583,929</u>	<u>\$258,952</u>	<u>\$2,167,457</u>	<u>\$2,208</u>	<u>\$ -0-</u>	



AGENCY REPLY





STATE OF MONTANA
DEPARTMENT OF HIGHWAYS

RECEIVED

March 24, 1977

MAR 24 1977

10:HJA

MONTANA LEGISLATIVE AUDITOR

Mr. Morris L. Brusett
Legislative Auditor
Office of the Legislative Auditor
State Capitol
Helena, Montana 59601

Re: Ernst and Ernst Audit

Dear Morris:

Attached is a memorandum which sets forth the Department's responses to the recommendations contained in the subject audit.

If there are further questions to be answered, please advise.

Very truly yours,

A handwritten signature in cursive ink, appearing to read "H. J. Anderson".
H. J. ANDERSON
Director of Highways

HJA/be

cc: Montana Highway Commissioners

Attachment

RECEIVED

MAR 25 1977

MONTANA LEGISLATIVE AUDITOR

INTER-DEPARTMENTAL MEMORANDUM

DEPARTMENT OF HIGHWAYS

To	H. J. Anderson, Director of Highways	Date	March 23, 1977
From	John L. Prebil, Administrator - Centralized Services Division	Subject:	Ernst & Ernst Audit Report

You have requested that I comment on the findings of Ernst & Ernst in their audit report for the period July 1, 1974 thru June 30, 1976. My comments are:

1. Recommendation: The Department should carefully consider the applicability of all accounting and reporting pronouncements. Consideration should be given to hiring a person to be specifically responsible during a transition period of designing financial statements in accordance with generally accepted accounting principles.

Answer: We will immediately endeavor to purchase all authoritative pronouncements. We hired an employee two years ago to assist in the accounting workload but his time has not been fully allocated to implementing this recommendation. We will reallocate his time to accomplish this recommendation.

2. Recommendation: The Department should institute an overall training program for key accounting employees.

Answer: We will comply with this recommendation immediately.

3. Recommendation: The accounting department should continue to monitor the use of and need for reports now being prepared.

Answer: We have sent questionnaires on our reports on an annual basis in the past and have discontinued many reports as a result of the questionnaires. We will continue to monitor the reports by publishing only those which are needed for management decisions or for financial disclosure.

4. Recommendation: All persons in the accounting office authorized to make accounting entries should be trained to making entries involving interfund accounts.

Answer: This item has given us no problem in the past; entries are guaranteed to be accurate. By using the computer to furnish us with the entries needed would be much simpler than educating all payroll preparation personnel, and equipment distribution personnel. We have no quarrel with training personnel in the accounting office on items produced in this office but the constant training of personnel in all of our other offices could result in improper entries, whereas the present method of using the computer is accurate.

5. Recommendation: The accounting office should not make accounting entries to equity accounts except in unusual and rare circumstances.

Answer: We will discontinue using the equity account for adjusting prior years adjustments and will establish a new general ledger account to handle these entries.

6. Recommendation: A management steering committee should be established to evaluate electronic data processing progress and discuss EDP problems. Also, in conjunction with the accounting division, the Data Processing Bureau should establish special training programs for presentation of EDP reports.

Answer: Both of these recommendations will be implemented in the very near future.

7. Recommendation: An allowance for possible doubtful accounts should be established.

Answer: The amount of bad debts generally amounts to less than \$7,500 per year and since the amount has been insignificant compared to over \$1 million billed annually we felt that it was not necessary to establish a reserve but only account for bad debts as they occur. We will implement this recommendation immediately.

8. Recommendation: Unreimbursed costs and reimbursements in excess of costs to be allocated to projects or other departments should be recognized as expenditures or revenues in the proper period.

Answer: Past auditors have brought this item to our attention and our standard reply was that the Federal Highway Administration demanded that we show on our books any overcharge on any rate charged their agency. Previous auditors have contacted the FHWA and they verified that was true. We have contacted that agency again and they have agreed to permit us to close the accounts involved at year end, provided that we keep a file on the overcharges or undercharges. Through their permission we will implement the auditor's recommendation.

9. Recommendation: Unreimbursed costs for construction work in disaster areas should be carefully monitored to determine final disposition of costs incurred.

Answer: Costs reported in this account have now been cleared. We will follow the recommendation whenever this account is used in the future.

10. Recommendation: Account balances related to the new building complex should be removed from the Earmarked Revenue Fund of the Department.

Answer: We will follow this recommendation. It was our belief that all transactions involving the earmarked revenue account should be properly

recorded in our books. The earmarked revenue fund has an obligation for the bond indebtedness of \$7,400,000 and we felt that it was proper to record this item on our books.

11. Recommendation: The Department should as soon as possible establish separate accounts to account for fixed assets.

Answer: We will implement this recommendation within the next month.

12. Recommendation: Receiving logs with columns for goods received, quantity, vendor name, date and the person's name who received the goods, should be prepared at each receiving location. These logs, together with appropriate invoices would be sent to the accounting office for processing. These procedures would help ensure that all goods received were placed in Highway inventory, and can be used to determine whether claims payable are recorded in the proper accounting period.

Answer: We were requested to look into this by the last auditor and we questioned the cost/benefit ratio of implementing this log, therefore we did not establish a log. We will make a more detailed study of this recommendation and if any benefit is derived we will implement the recommendation. We hesitate to add another report just for the sake of having a report.

13. Recommendation: The Department's accounting system should be designed to show revenues and expenditures, by type, accumulated between the beginning of a fiscal year and the date reports are prepared.

Answer: Our postings are made each month under each month's heading but a total is not shown for a month or the fiscal year on any accumulative account. Rather, the account balance is added to or subtracted from on each month. We will redesign our general ledger sheets to accommodate this recommendation. It is questionable if this recommendation will aid our reporting and/or accounting system.

14. Recommendation: The detail ledger showing individual insurance payments made in advance by retirees should be reconciled to the general ledger on a monthly basis.

Answer: We have accomplished this since last July.

15. Recommendation: Details of the city and county fund should be reconciled to the general ledger on a continuing basis.

Answer: The reports prepared have been reconciled to the general ledger, but at year end in 1975 the report was prepared before the books were completely closed and as a result the June 1975 city and county report did not reflect all of the year end expenditures.

This has not been the practice in the past and will not be in the future. The June, 1976 report, as well as all monthly reports have been prepared correctly.

16. Recommendation: 1. Distribution of all G.V.W. collections on a timely basis will give the Department's Earmarked Revenue Fund and other governmental units a more timely picture of revenue trends.
2. The Earmarked Revenue Fund should institute the policy of accordance with generally accepted accounting procedures.

Answer: 1. Steps have been taken to receive computer print-out statements in a more timely manner and with those print-outs we will be in a position to clear the accounts on a monthly cycle.

2. Instructions were issued by the Department of Administration that expenses would be accrued but income would not; therefore, the State would operate on a modified accrual basis accounting system. We have complied with these instructions. In order to comply with the auditor's recommendations we will disregard the Department of Administration's instructions. We agree that it is generally accepted accounting procedure to accrue income, and we will do so at the close of the 1977 fiscal year.

17. Recommendation: G.V.W. should consider having its own keypunch operator rather than having to wait for available time from the Data Processing Bureau.

Answer: The G.V.W. keypunching became a problem because that division did have 2 keypunchers who resigned and replacements could not be hired for some time; therefore, the keypunching work was transferred to the Data Processing Bureau. G.V.W. keypunching has been assigned top priority in the Data Processing Bureau and the data seems to be flowing quite smoothly. We do feel that when the Department moves to its new building that keypunchers should be reassigned to G.V.W. Division.

18. Recommendation: Special fuel permit fine collections should be sent directly to the highway accounting office with a report being sent to the G.V.W. office.

Answer: The newly adopted lower court accounting system corrects this problem. Under the new system all monies collected by justices of peace will be deposited with county treasurers who will remit the amounts to the state treasurer. Reports will be sent to the G.V.W. office of all deposits.

19. Recommendation: Unused G.V.W. permit tickets should be more carefully controlled, if not destroyed.

Answer: We have instituted a policy to cut in half, by machine cutting, each book of unused tickets. We will return the numbered portion and destroy the unnumbered portion.

20. Recommendation: Future payroll accruals should be properly recorded as an accrued liability.

Answer: While preparing our payroll entry, we made a mental error by charging the entire payroll to cash rather than a portion to cash and a portion to the accrued payroll liability account. This was a human error and our procedures call for accruing all unpaid costs at year end.

21. Recommendation: The record system for reporting sick leave should be adjusted to provide information regarding both emergency and regular sick leave.

Answer: Procedures were adopted on January 1, 1977 to implement this recommendation.

22. Recommendation: The completed payroll checks and payroll journal should be sent to the division manager. The journal could be reviewed by the payroll clerk. The checks, however, should be distributed by the division manager or another designated employee, but not the payroll clerk or any other employee associated with the hiring process or with the handling of originating payroll records.

Answer: We will implement this recommendation after we complete a study of various methods of distributing the pay checks and arrive at a suitable method for distributing them.

23. Recommendation: Returned W-2 Forms should be investigated and followed up by employees other than the payroll department.

Answer: We will comply with this recommendation.

24. Recommendation: Before being keypunched, all journal entries should be properly reviewed by an authorized person.

Answer: At the beginning of this fiscal year we assigned an accountant to approve of any journal voucher prepared for under \$5,000.00 and require my approval for any over \$5,000.00.

